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C O N F I D E N T I A L SECTION 01 OF 03 SAO PAULO 000679

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TAGS: PGOV ECON EFIN EINV ETRD BR

SUBJECT: ECONOMIC CRISIS HELPS SERRA POSITION FOR 2010

REF: SAO PAULO 581

Classified By: Consul General Thomas White; Reasons 1.4 (b) and (d).

¶1. (C) Summary: The PSDB leadership sees an opportunity for their party as the ongoing global economic crisis hits Brazil. In this context, Sao Paulo state governor Jose Serra, the most likely PSDB nominee right now, has started a campaign of economic activism at the state level, promoting programs to strengthen the economy, improve mass transit, and generate employment in both Sao Paulo state and in the city. Serra's efforts would appear designed to create a formidable track record for his run in 2010 and demonstrate his capacity to be an effective manager and first-responder to any economic crisis. The Sao Paulo Governor has complemented these moves with efforts to reach out to other parties, building a strong and diverse support base in his home region. End Summary.

¶2. (C) Sao Paulo Governor Jose Serra's campaign to position himself to run for Brazil's presidency in 2010 continues in earnest. The flagship of his efforts was his successful effort to get his ally, incumbent Sao Paulo Mayor Gilberto Kassab (DEM party), re-elected (Ref). Kassab's landslide win over PT candidate Marta Suplicy was important, but should not obscure the other deft moves Serra has been making to both secure the PSDB nomination and win Brazil's presidency in 2010. Serra seeks to present himself as an effective manager who can protect Brazil's prosperity against the ongoing global economic crisis. These efforts have intensified since Kassab's mayoral victory on October 26.

The Context: Opportunity in Economic Difficulty

¶3. (C) Contacts in the PSDB say that the ongoing global economic crisis will set the context for the 2010 elections. They expect the effects of the crisis to hit Brazil hard in the first trimester of 2009 and continue into early 2010. So far, they argue, President Lula and his economic team have not been challenged. They inherited a sound political-economy from PSDB President Cardoso and have only made slight modifications, maintaining an orthodox macroeconomic policy. The crisis will test President Lula's

economic team as well as his own sky-high popularity, which is a product of the President's considerable charisma, and the economic good times during which he's governed and, most recently, of the fact that Brazilians felt only minimal effects from the global financial crisis--something certain to change. PSDB insiders say that the coming economic difficulties will create an opening for Governor Serra to present himself as an excellent manager who can protect Brazil's prosperity during a difficult global economic situation. They also see the crisis, and the Governor's response, as an opportunity for Serra to win over the financial community, which has sometimes viewed him with skepticism. When the crisis hits in full force, reluctant financiers will see virtue in the kind of economy-supporting state activism that Serra champions, according to Serra advisor Luis Henrique Reis Lobo (protect).

Serra Establishes his Bona Fides: A Mini-New Deal

¶4. (C) Sao Paulo Governor Serra has been moving on a variety of fronts to establish his managerial and programmatic bona fides for the electorate: shoring up state finances, extending credit to industry, and building infrastructure. His approach, which includes a heavy dose of state activism, represents a likely rehearsal of the measures he might take as President. Taken together, his initiatives look like a kind of mini-New Deal for Sao Paulo State. Among the actions taken:

--Getting Resources: Serra oversaw the sale of the Sao Paulo state bank, Nossa Caixa, to Banco do Brazil for USD 2.2

SAO PAULO 00000679 002 OF 003

billion on November 20, a move that raised significant cash for the Sao Paulo state government.

--Extending the Metro to Sao Paulo's Periphery: Serra first announced his "Plan for the Expansion of Metropolitan Transport 2007-2010" last June. He proposed to build a modern and efficient transportation system for Sao Paulo through massive investment of approximately USD 8 billion financed from a variety of sources, including the Interamerican Bank, the World Bank and the Japan Bank of International Cooperation. The Governor followed this up on December 5 with an announcement to add an additional branch to the metro that would construct 8.4 kilometers of new lines and 17 new stations, extending the metro into the northern part of Sao Paulo. The resulting project will provide transport for 650,000 commuters a day and will cost approximately USD 1 billion. This would establish the first metro links between the city center and two outlying peripheral regions of the city. In announcing this latest transport link with Sao Palo's outer north, Serra said, "We sold Nossa Caixa, a bank we didn't need, and we traded it for a metro."

--Developing a State Economic Promotion Agency: Serra announced on November 20 that the Sao Paulo state government would use about USD 500 million from the sale of Nossa Caixa to create a new, state-level economic promotion agency, to be formed in April 2009. The new state entity will focus on state investments primarily to promote employment as well as make improvements in transport, health, education, and security.

--Developing a State Investment Agency: Serra announced the creation of a state investment agency, Invest Sao Paulo, with USD 5 billion on December 8. The agency's resources will support 40 projects in diverse sectors of the Sao Paulo state economy with the idea of encouraging investment. It will support diverse projects, including road building, metro improvements as well as health and education. It will be run by a board composed of government officials and private business persons. (Comment: Some of Serra's programs appear overlapping and duplicative. Nonetheless, the multiplicity of start-up announcements gives the Governor both media

placement and excellent momentum. End Comment.)

--Extending Lines of Credit: Serra extended a line of credit of approximately USD 600 million to the machine tools and auto-parts industry on December 12. The plan also postpones certain taxes owed by industrialists and provides tax rebates to small businesses. The Governor announced his program to stimulate industry the day after President Lula put forward a similar stimulus program at the national level.

The Counter-Dilma

¶ 15. (C) Serra's recent actions appear designed to give him a track record to use against his likely opponent, President Lula's Chief of Staff, Dilma Rousseff. Rousseff oversees Brazil's national-level program for public-private partnerships to accelerate economic growth (PAC), an opportunity that observers feel was given to her precisely to burnish her credentials as a potential presidential candidate. In the meantime, Serra is creating an impressive history of state-level accomplishments that could counter Rousseff's achievement as PAC Director.

¶ 16. (SBU) Recent public opinion polls would appear to reflect Serra's strengthened position. A November 25 Datafolha survey that matched Serra against a variety of candidates had him coming in first place in all scenarios with varying levels of support depending on the depth of the field. Probable PT Rival Dilma Rousseff is well behind in these polls, although none of the current scenarios have them head to head and the number of "don't know" and blank answers

SAO PAULO 00000679 003 OF 003

represents a significant percentage of the total. (Comment: Polling almost two years out from an election should always be viewed with caution, but Brazilians are particularly fickle in their affinities. Some 90 percent of Brazilian voters have no party affiliation, and the recent municipal elections saw many candidates go from footnote to front-runner over a matter of weeks prior to voting day. End Comment.)

Casting a Wide Net for Allies

¶ 17. (C) Serra has complemented his strategy of state-based economic activism with a successful effort to engage a wide range of political allies. On the right, he has a strong partnership with DEM leader and Sao Paulo Mayor Gilberto Kassab. On the left, his party is allied with the Popular Socialist Party, a descendent of the once pro-Soviet branch of Brazil's communist party. (The other formerly pro-Chinese faction, the Communist Party of Brazil, is allied with President Lula and provided Marta Suplicy's running mate in the Sao Paulo Mayoral race.) Finally, Serra has built a strong alliance with Sao Paulo PMDB leader and former Sao Paulo Governor Orestes Quercia. Quercia told Poloff that he does not trust the PT, calling it a party "that doesn't keep its promises." It is widely thought that Serra has promised to support Quercia in the latter's quest to become a Senator. While no one ally can deliver the regionally-based PMDB, Quercia's support and the backing of the Sao Paulo faction of the party give Serra an important inroad with this key group. (Comment: The PMDB won more of the recent municipal elections than any other party in the country and can use these bully pulpits in support of whoever becomes the party's preferred candidate in 2010. Although currently allied with Lula and the PT at the national level, without any obvious candidate of their own, PMDB leaders are keeping their options open for 2010. End Comment.)

PSDB Leadership and the Quest for the "Dream Ticket"

¶ 18. (C) Despite Serra's smart moves and recent political wins, he still faces a rival in his own party in the form of Minas Gerais Governor Aecio Neves. Behind the scenes, former President Fernando Henrique Cardoso is reportedly working

hard to pull together a PSDB "dream ticket," which would launch Serra as the party's presidential candidate with Neves running as his Vice President. A recent report in Estado de Sao Paulo suggested that, in an effort to gain Neves' buy-in to serve as his running mate, Serra has offered to support a constitutional amendment against re-election beginning with the 2010 election, which would ensure, should Serra win, that Neves could run as his successor. Given Neves' relative youth (he is only 48 while Serra is 66), the dream ticket could have appeal for Neves, helping both his Party and paving the way for his own future candidacy. So far, however, Neves has given no indication of interest in such a deal.

Comment: The Man to Beat

¶9. (C) Serra has followed his Sao Paulo Mayor's race victory with a series of moves that establish him as an efficient manager and first-responder to the early stages of the financial crisis, which has begun to hit Brazil. Poll numbers appear to indicate that his moves in creating a positive track record of activism in confronting the economic crisis are paying off. Though obstacles remain, Serra is off to a strong start in his campaign to succeed President Lula.
End Comment.

¶10. (U) This cable was coordinated/cleared by Embassy Brasilia.

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